

AMENDED IN ASSEMBLY APRIL 8, 2014

CALIFORNIA LEGISLATURE—2013–14 REGULAR SESSION

ASSEMBLY BILL

No. 1564

Introduced by Assembly Member V. Manuel Pérez

January 29, 2014

An act to add Article 4.5 (commencing with Section 12097) to Chapter 1.6 of Part 2 of Division 3 of Title 2 of the Government Code, and to amend Sections 17052.12 and 23609 of, and to add Section 19535 to, the Revenue and Taxation Code, relating to taxation, and making an appropriation therefor.

LEGISLATIVE COUNSEL'S DIGEST

AB 1564, as amended, V. Manuel Pérez. Income taxes: research and development credit: credit sale and purchase.

The Personal Income Tax Law and the Corporation Tax Law allow various credits against the taxes imposed by those laws, including a credit for a percentage of specified research expenses.

This bill would increase that percentage by 3% each taxable year for 5 taxable years and then return to the current rate. ~~This bill would limit the credit to a 10-year carryover period.~~ This bill would create a Research and Development Tax Credit Trade Program, which the Governor's Office of Business and Economic Development (GO-Biz) would administer to authorize taxpayers to purchase and sell the credits. This bill would appropriate a portion of the money made from the sale of the credits to GO-Biz and the Franchise Tax Board for the costs incurred by the agencies in administering the program. This bill would impose specified auditing requirements on the Franchise Tax Board related to this credit, as specified.

~~This bill would include a change in state statute that would result in a taxpayer paying a higher tax within the meaning of Section 3 of Article XIII A of the California Constitution, and thus would require for passage the approval of 2/3 of the membership of each house of the Legislature.~~

Vote: 2/3. Appropriation: yes. Fiscal committee: yes.
State-mandated local program: no.

The people of the State of California do enact as follows:

- 1 SECTION 1. The Legislature finds and declares the following:
- 2 (a) California’s greatest economic asset is its diverse economy
- 3 that supports key industry clusters that rely upon innovation to
- 4 compete globally.
- 5 (b) California is uniquely situated to benefit from increasing
- 6 research and development tax credits because of California’s world
- 7 renowned academic institutions, industry clusters, and diverse
- 8 population that attracts worldwide talent.
- 9 (c) Recent studies conducted by the Public Policy Institute of
- 10 California ranked California fourth in the nation in entrepreneurial
- 11 energy and second in the nation in innovation capacity. However,
- 12 California was ranked as having only the 43rd most favorable
- 13 corporate tax structure. This ~~low ranking~~ *ranking* artificially reduces
- 14 the capacity of research and development that could occur in the
- 15 state because companies are more likely to expand to other states
- 16 ~~or counties~~ *countries* where they will be taxed at a lower level.
- 17 (d) Creating an environment rich in research and development
- 18 spawns the growth of manufacturing. In the last 10 years, California
- 19 has declined from the sixth largest economy in the world to the
- 20 ninth, which is behind Brazil. During that time, manufacturing
- 21 declined in California from 1.865 million jobs to 1.257 million
- 22 jobs.
- 23 (e) California needs to invest in the innovation economy by
- 24 eliminating the roadblocks in state law and regulations and by
- 25 developing a tax system that rewards capital expenditures in order
- 26 to ensure that the private sector will invest financial capital and
- 27 intellectual capital in California.
- 28 (f) California needs to support the creation of new manufacturing
- 29 jobs created by the private sector in the innovation economy with
- 30 a highly skilled workforce.
- 31 SEC. 2. It is the intent of the Legislature to do the following:

1 (a) Incrementally increase the research and development tax
2 credits under the Personal Income Tax Law and the Corporation
3 Tax Law up to 15 percent for a five-year period.

4 ~~(b) Reduce California's research and development tax credits~~
5 ~~by creating a 10-year carryover maximum, focusing the credits on~~
6 ~~startup businesses.~~

7 ~~(e)~~

8 (b) Create new and clearly defined auditing procedures for the
9 Franchise Tax Board relating to this credit to allow taxpayers
10 claiming a research and development tax credit to defend their
11 research and development activities.

12 SEC. 3. Article 4.5 (commencing with Section 12097) is added
13 to Chapter 1.6 of Part 2 of Division 3 of Title 2 of the Government
14 Code, to read:

15
16 Article 4.5. The Research and Development Tax Credit Trade
17 Program
18

19 12097. The Governor's Office of Business and Economic
20 Development (GO-Biz) shall develop and administer a program
21 to allow the sale or purchase of research and development tax
22 credits allowed under Sections 17052.12 and 23609 of the Revenue
23 and Taxation Code. GO-Biz shall create an Internet Web site
24 through which approved taxpayers may, by January 1, 2017, make
25 such sale or purchase.

26 (a) The Franchise Tax Board shall notify GO-Biz quarterly of
27 all taxpayers that claim a credit under Sections 17052.12 and 23609
28 of the Revenue and Taxation Code, and the amount of credit
29 claimed.

30 (b) A taxpayer may request approval by GO-Biz to sell or
31 purchase a credit.

32 (c) GO-Biz shall approve a taxpayer before that taxpayer may
33 sell or purchase the credits.

34 (1) GO-Biz shall approve a taxpayer to sell its credits if that
35 taxpayer has all of the following:

36 (A) A facility in which research and development occurs in the
37 state.

38 (B) Less than fifty million dollars (\$50,000,000) in earnings
39 before income tax, depreciation, and amortization.

1 (C) Unused research and development tax credits from a
2 previous taxable year.

3 (2) GO-Biz shall approve a taxpayer to purchase a research and
4 development tax credit if all of the following requirements are
5 met:

6 (A) The taxpayer has had qualified research expenses, as defined
7 in Sections 17052.12 and 23609 of the Revenue and Taxation Code
8 and Section 41 of the Internal Revenue Code, within the past five
9 years.

10 (B) The taxpayer conducts a trade or business in the state.

11 (d) If a taxpayer is approved, GO-Biz shall create an online
12 account for the taxpayer to allow the taxpayer to log into the
13 Internet Web site to sell or purchase the credits.

14 (e) A taxpayer shall not be approved to sell or purchase more
15 than five million dollars (\$5,000,000) in unused research and
16 development tax credits per taxable year.

17 (f) If the taxpayer does not reinvest the money received from
18 the sale of the credit into the taxpayer's trade or business or if the
19 purchased credits reduce the taxpayer's tax liability by more than
20 50 percent, any remaining unapplied credit shall be canceled and
21 any previously applied credit that was not reinvested or that
22 exceeds 50 percent of the taxpayer's tax liability shall be
23 recaptured, and the taxpayer shall be liable for any increase in tax
24 attributable to the recapture of any credit previously allowed under
25 this section.

26 (g) The price of the credit shall be based on the open-market
27 demand.

28 (h) GO-Biz shall notify the Franchise Tax Board of each sale
29 or purchase of a credit, the identity of the taxpayer selling the
30 credit, the identity of the taxpayer that purchased the credit, and
31 the amount of the credit sold quarterly. The Franchise Tax Board
32 shall review this information to ensure that a credit is not being
33 used multiple times.

34 12097.1. (a) There is hereby established in the State Treasury
35 the Research and Development Tax Credit Trade Fund.

36 (b) (1) Until GO-Biz has been fully reimbursed for its costs of
37 developing, creating, and starting the Research and Development
38 Tax Credit Trade Program, *moneys in an amount equal to 15*
39 *percent of the face value of each credit sold or purchased on the*
40 *Internet Web site established by GO-Biz shall be deposited into*

1 the Research and Development Tax Credit Trade Fund for the
2 purpose of funding this program pursuant to Section 12097, and
3 appropriated as follows:

4 (A) ~~Thirteen~~ *Moneys in an amount equal to 13 percent of the*
5 *face value of each credit to GO-Biz for the administrative and*
6 *start-up costs of implementing this program.*

7 (B) ~~Two~~ *Moneys in an amount equal two percent of the face*
8 *value of each credit to the Franchise Tax Board for the*
9 *administrative costs of implementing this program.*

10 (2) ~~The remaining 85~~ *Eighty-five percent of the face value of*
11 *each credit may be used as a credit against the “net tax” or “tax,”*
12 *as applicable of the taxpayer that purchased the credit.*

13 (c) (1) Once GO-Biz has been fully reimbursed for its costs of
14 developing, creating, and starting this program, *moneys in an*
15 *amount equal to 5 percent of the face value of each credit sold*
16 *through the Internet Web site established by GO-Biz shall be*
17 *deposited into the Research and Development Tax Credit Trade*
18 *Fund for the purpose of funding the Research and Development*
19 *Tax Credit Trade Program pursuant to Section 12097, and*
20 *appropriated as follows:*

21 (A) ~~Three~~ *Moneys in an amount equal to three percent of the*
22 *face value of each credit to GO-Biz for the administrative costs of*
23 *implementing this program.*

24 (B) ~~Two~~ *Moneys in an amount equal to two percent of the face*
25 *value of each credit to the Franchise Tax Board for the*
26 *administrative costs of implementing this program.*

27 (2) ~~The remaining 95~~ *Ninety-five percent of the amount of each*
28 *credit may be used as a credit against the “net tax” or “tax,” as*
29 *applicable of the taxpayer that purchased the credit.*

30 SEC. 4. Section 17052.12 of the Revenue and Taxation Code
31 is amended to read:

32 17052.12. For each taxable year beginning on or after January
33 1, 1987, there shall be allowed as a credit against the “net tax” (as
34 defined by Section 17039) for the taxable year an amount
35 determined in accordance with Section 41 of the Internal Revenue
36 Code, except as follows:

37 (a) For each taxable year beginning before January 1, 1997, the
38 reference to “20 percent” in Section 41(a)(1) of the Internal
39 Revenue Code is modified to read “8 percent.”

- 1 (b) (1) For each taxable year beginning on or after January 1,
2 1997, and before January 1, 1999, the reference to “20 percent”
3 in Section 41(a)(1) of the Internal Revenue Code is modified to
4 read “11 percent.”
- 5 (2) For each taxable year beginning on or after January 1, 1999,
6 and before January 1, 2000, the reference to “20 percent” in Section
7 41(a)(1) of the Internal Revenue Code is modified to read “12
8 percent.”
- 9 (3) For each taxable year beginning on or after January 1, 2000,
10 and before January 1, 2014, the reference to “20 percent” in Section
11 41(a)(1) of the Internal Revenue Code is modified to read “15
12 percent.”
- 13 (4) For each taxable year beginning on or after January 1, 2014,
14 and before January 1, 2015, the reference to “20 percent” in Section
15 41(a)(1) of the Internal Revenue Code is modified to read “18
16 percent.”
- 17 (5) For each taxable year beginning on or after January 1, 2015,
18 and before January 1, 2016, the reference to “20 percent” in Section
19 41(a)(1) of the Internal Revenue Code is modified to read “21
20 percent.”
- 21 (6) For each taxable year beginning on or after January 1, 2016,
22 and before January 1, 2017, the reference to “20 percent” in Section
23 41(a)(1) of the Internal Revenue Code is modified to read “24
24 percent.”
- 25 (7) For each taxable year beginning on or after January 1, 2017,
26 and before January 1, 2018, the reference to “20 percent” in Section
27 41(a)(1) of the Internal Revenue Code is modified to read “27
28 percent.”
- 29 (8) For each taxable year beginning on or after January 1, 2018,
30 and before January 1, 2019, the reference to “20 percent” in Section
31 41(a)(1) of the Internal Revenue Code is modified to read “30
32 percent.”
- 33 (9) For each taxable year beginning on or after January 1, 2019,
34 the reference to “20 percent” in Section 41(a)(1) of the Internal
35 Revenue Code is modified to read “15 percent.”
- 36 (c) Section 41(a)(2) of the Internal Revenue Code shall not
37 apply.
- 38 (d) “Qualified research” shall include only research conducted
39 in California.

1 (e) In the case where the credit allowed under this section
2 exceeds the “net tax,” the excess may be carried over to reduce
3 the “net tax” in the following year, and succeeding ~~nine~~ years if
4 necessary, until the credit has been exhausted.

5 (f) (1) With respect to any expense paid or incurred after the
6 operative date of Section 6378, Section 41(b)(1) of the Internal
7 Revenue Code is modified to exclude from the definition of
8 “qualified research expense” any amount paid or incurred for
9 tangible personal property that is eligible for the exemption from
10 sales or use tax provided by Section 6378.

11 (2) For each taxable year beginning on or after January 1, 1998,
12 the reference to “Section 501(a)” in Section 41(b)(3)(C) of the
13 Internal Revenue Code, relating to contract research expenses, is
14 modified to read “this part or Part 11 (commencing with Section
15 23001).”

16 (g) (1) For each taxable year beginning on or after January 1,
17 2000:

18 (A) The reference to “3 percent” in Section 41(c)(4)(A)(i) of
19 the Internal Revenue Code is modified to read “one and forty-nine
20 hundredths of one percent.”

21 (B) The reference to “4 percent” in Section 41(c)(4)(A)(ii) of
22 the Internal Revenue Code is modified to read “one and
23 ninety-eight hundredths of one percent.”

24 (C) The reference to “5 percent” in Section 41(c)(4)(A)(iii) of
25 the Internal Revenue Code is modified to read “two and forty-eight
26 hundredths of one percent.”

27 (2) Section 41(c)(4)(B) shall not apply and in lieu thereof an
28 election under Section 41(c)(4)(A) of the Internal Revenue Code
29 may be made for any taxable year of the taxpayer beginning on or
30 after January 1, 1998. That election shall apply to the taxable year
31 for which made and all succeeding taxable years unless revoked
32 with the consent of the Franchise Tax Board.

33 (3) Section 41(c)(7) of the Internal Revenue Code, relating to
34 gross receipts, is modified to take into account only those gross
35 receipts from the sale of property held primarily for sale to
36 customers in the ordinary course of the taxpayer’s trade or business
37 that is delivered or shipped to a purchaser within this state,
38 regardless of f.o.b. point or any other condition of the sale.

39 (4) Section 41(c)(5) of the Internal Revenue Code, relating to
40 election of alternative simplified credit, shall not apply.

1 (h) Section 41(h) of the Internal Revenue Code, relating to
2 termination, shall not apply.

3 (i) Section 41(g) of the Internal Revenue Code, relating to
4 special rule for passthrough of credit, is modified by each of the
5 following:

6 (1) The last sentence shall not apply.

7 (2) If the amount determined under Section 41(a) of the Internal
8 Revenue Code for any taxable year exceeds the limitation of
9 Section 41(g) of the Internal Revenue Code, that amount may be
10 carried over to other taxable years under the rules of subdivision
11 (e); except that the limitation of Section 41(g) of the Internal
12 Revenue Code shall be taken into account in each subsequent
13 taxable year.

14 (j) Section 41(a)(3) of the Internal Revenue Code shall not apply.

15 (k) Section 41(b)(3)(D) of the Internal Revenue Code, relating
16 to amounts paid to eligible small businesses, universities, and
17 federal laboratories, shall not apply.

18 (l) Section 41(f)(6), relating to energy research consortium,
19 shall not apply.

20 (m) A taxpayer may sell a credit allowed under this section
21 pursuant to Article 4.5 (commencing with Section 12097) of
22 Chapter 1.6 of ~~Part~~, *Part 2* of Division 3 of Title 2 of the
23 Government Code.

24 SEC. 5. Section 19535 is added to the Revenue and Taxation
25 Code, to read:

26 19535. (a) The Franchise Tax Board shall perform the
27 following audit procedures if a taxpayer filed for a credit under
28 Section 17052.12 or 23609 and was not allowed that credit:

29 (1) Use a risk-based approach to conduct an audit. The
30 risk-based approach shall focus on identifying areas of a taxpayer's
31 business or trade in which there may be subjectivity in determining
32 whether an employee of the taxpayer is performing qualified
33 research or nonqualified research, and what percentage of that
34 employee's time is devoted to performing qualified research.

35 (2) Require a general explanation of the taxpayer's trade or
36 business, the role of research and development in the trade or
37 business, the development of new and improved products,
38 processes, and software from the taxpayer.

39 (3) Determine whether the Internal Revenue ~~Services~~ *Service*
40 has conducted an examination of the credit allowed under Section

1 41 of the Internal Revenue Code and request a copy of the audit
2 report. If the Internal Revenue ~~Services~~ *Service* has conducted an
3 examination, the Franchise Tax Board shall rely upon the findings
4 of the examination, subject to verifying that the research activities
5 and costs were incurred in state.

6 (4) Conduct a physical tour of the taxpayer's facilities and
7 interview employees of the taxpayer that are performing qualified
8 research. A physical tour should be conducted prior to arriving at
9 a determination that a taxpayer's activities do not qualify as
10 qualified research, as defined in Sections 17052.12 and 23609.
11 The tour shall include the area in which research is performed and
12 follow a product or process through its life cycle beginning with
13 development and ending in production.

14 (5) Identify the types of employees dedicated to research,
15 production, or administrative duties, or a mixture of any of those
16 activities.

17 (b) The Franchise Tax Board may perform the following audit
18 procedures if a taxpayer filed for a credit under Section 17052.12
19 or 23609 and was not allowed that credit and the auditor deems it
20 necessary:

21 (1) Ask the taxpayer to provide examples of research projects
22 from the examination years and to describe projects that are
23 currently under development.

24 (2) Ask the taxpayer to explain each step of the development
25 process, where mixed-services are performed, and distinguish
26 between production or administration functions and research.

27 (c) If the Franchise Tax Board determines a particular expense
28 to not be a qualified research expenditure, a taxpayer shall be
29 allowed an opportunity to provide additional supporting records.
30 If an adjustment in whether an expense is considered a qualified
31 research expense is necessary based on the ~~taxpayers~~ *taxpayer's*
32 additional supporting records, the Franchise Tax Board shall
33 explain and document the discrepancy. An adjustment based upon
34 mere criticism of a taxpayer's workpapers, study, methods, or
35 vague disallowance for law of substantiation, without actual
36 information or evidence that contradict a taxpayer's documents or
37 other evidence shall not be upheld. A lack of substantiation shall
38 be a valid reason for disallowing a credit when the taxpayer only
39 submits vague testimony.

1 SEC. 6. Section 23609 of the Revenue and Taxation Code is
2 amended to read:

3 23609. For each taxable year beginning on or after January 1,
4 1987, there shall be allowed as a credit against the “tax” (as defined
5 by Section 23036) an amount determined in accordance with
6 Section 41 of the Internal Revenue Code, except as follows:

7 (a) For each taxable year beginning before January 1, 1997,
8 both of the following modifications shall apply:

9 (1) The reference to “20 percent” in Section 41(a)(1) of the
10 Internal Revenue Code is modified to read “8 percent.”

11 (2) The reference to “20 percent” in Section 41(a)(2) of the
12 Internal Revenue Code is modified to read “12 percent.”

13 (b) (1) For each taxable year beginning on or after January 1,
14 1997, and before January 1, 1999, both of the following
15 modifications shall apply:

16 (A) The reference to “20 percent” in Section 41(a)(1) of the
17 Internal Revenue Code is modified to read “11 percent.”

18 (B) The reference to “20 percent” in Section 41(a)(2) of the
19 Internal Revenue Code is modified to read “24 percent.”

20 (2) For each taxable year beginning on or after January 1, 1999,
21 and before January 1, 2000, both of the following shall apply:

22 (A) The reference to “20 percent” in Section 41(a)(1) of the
23 Internal Revenue Code is modified to read “12 percent.”

24 (B) The reference to “20 percent” in Section 41(a)(2) of the
25 Internal Revenue Code is modified to read “24 percent.”

26 (3) For each taxable year beginning on or after January 1, 2000,
27 and before January 1, 2014, both of the following shall apply:

28 (A) The reference to “20 percent” in Section 41(a)(1) of the
29 Internal Revenue Code is modified to read “15 percent.”

30 (B) The reference to “20 percent” in Section 41(a)(2) of the
31 Internal Revenue Code is modified to read “24 percent.”

32 (4) For each taxable year beginning on or after January 1, 2014,
33 and before January 1, 2015, both of the following shall apply:

34 (A) The reference to “20 percent” in Section 41(a)(1) of the
35 Internal Revenue Code is modified to read “18 percent.”

36 (B) The reference to “20 percent” in Section 41(a)(2) of the
37 Internal Revenue Code is modified to read “27 percent.”

38 (5) For each taxable year beginning on or after January 1, 2015,
39 and before January 1, 2016, both of the following shall apply:

1 (A) The reference to “20 percent” in Section 41(a)(1) of the
2 Internal Revenue Code is modified to read “21 percent.”

3 (B) The reference to “20 percent” in Section 41(a)(2) of the
4 Internal Revenue Code is modified to read “30 percent.”

5 (6) For each taxable year beginning on or after January 1, 2016,
6 and before January 1, 2017, both of the following shall apply:

7 (A) The reference to “20 percent” in Section 41(a)(1) of the
8 Internal Revenue Code is modified to read “24 percent.”

9 (B) The reference to “20 percent” in Section 41(a)(2) of the
10 Internal Revenue Code is modified to read “33 percent.”

11 (7) For each taxable year beginning on or after January 1, 2017,
12 and before January 1, 2018, both of the following shall apply:

13 (A) The reference to “20 percent” in Section 41(a)(1) of the
14 Internal Revenue Code is modified to read “27 percent.”

15 (B) The reference to “20 percent” in Section 41(a)(2) of the
16 Internal Revenue Code is modified to read “36 percent.”

17 (8) For each taxable year beginning on or after January 1, 2018,
18 and before January 1, 2019, both of the following shall apply:

19 (A) The reference to “20 percent” in Section 41(a)(1) of the
20 Internal Revenue Code is modified to read “30 percent.”

21 (B) The reference to “20 percent” in Section 41(a)(2) of the
22 Internal Revenue Code is modified to read “39 percent.”

23 (9) For each taxable year beginning on or after January 1, 2019,
24 both of the following shall apply:

25 (A) The reference to “20 percent” in Section 41(a)(1) of the
26 Internal Revenue Code is modified to read “15 percent.”

27 (B) The reference to “20 percent” in Section 41(a)(2) of the
28 Internal Revenue Code is modified to read “24 percent.”

29 (c) (1) With respect to any expense paid or incurred after the
30 operative date of Section 6378, Section 41(b)(1) of the Internal
31 Revenue Code is modified to exclude from the definition of
32 “qualified research expense” any amount paid or incurred for
33 tangible personal property that is eligible for the exemption from
34 sales or use tax provided by Section 6378.

35 (2) “Qualified research” and “basic research” shall include only
36 research conducted in California.

37 (d) The provisions of Section 41(e)(7)(A) of the Internal
38 Revenue Code, shall be modified so that “basic research,” for
39 purposes of this section, includes any basic or applied research
40 including scientific inquiry or original investigation for the

1 advancement of scientific or engineering knowledge or the
2 improved effectiveness of commercial products, except that the
3 term does not include any of the following:

4 (1) Basic research conducted outside California.

5 (2) Basic research in the social sciences, arts, or humanities.

6 (3) Basic research for the purpose of improving a commercial
7 product if the improvements relate to style, taste, cosmetic, or
8 seasonal design factors.

9 (4) Any expenditure paid or incurred for the purpose of
10 ascertaining the existence, location, extent, or quality of any deposit
11 of ore or other mineral (including oil and gas).

12 (e) (1) In the case of a taxpayer engaged in any
13 biopharmaceutical research activities that are described in codes
14 2833 to 2836, inclusive, or any research activities that are described
15 in codes 3826, 3829, or 3841 to 3845, inclusive, of the Standard
16 Industrial Classification (SIC) Manual published by the United
17 States Office of Management and Budget, 1987 edition, or any
18 other biotechnology research and development activities, the
19 provisions of Section 41(e)(6) of the Internal Revenue Code shall
20 be modified to include both of the following:

21 (A) A qualified organization as described in Section
22 170(b)(1)(A)(iii) of the Internal Revenue Code and owned by an
23 institution of higher education as described in Section 3304(f) of
24 the Internal Revenue Code.

25 (B) A charitable research hospital owned by an organization
26 that is described in Section 501(c)(3) of the Internal Revenue Code,
27 is exempt from taxation under Section 501(a) of the Internal
28 Revenue Code, is not a private foundation, is designated a
29 “specialized laboratory cancer center,” and has received Clinical
30 Cancer Research Center status from the National Cancer Institute.

31 (2) For purposes of this subdivision:

32 (A) “Biopharmaceutical research activities” means those
33 activities that use organisms or materials derived from organisms,
34 and their cellular, subcellular, or molecular components, in order
35 to provide pharmaceutical products for human or animal
36 therapeutics and diagnostics. Biopharmaceutical activities make
37 use of living organisms to make commercial products, as opposed
38 to pharmaceutical activities that make use of chemical compounds
39 to produce commercial products.

1 (B) “Other biotechnology research and development activities”
2 means research and development activities consisting of the
3 application of recombinant DNA technology to produce
4 commercial products, as well as research and development
5 activities regarding pharmaceutical delivery systems designed to
6 provide a measure of control over the rate, duration, and site of
7 pharmaceutical delivery.

8 (f) In the case where the credit allowed by this section exceeds
9 the “tax,” the excess may be carried over to reduce the “tax” in
10 the following year, and succeeding ~~nine~~ years if necessary, until
11 the credit has been exhausted.

12 (g) For each taxable year beginning on or after January 1, 1998,
13 the reference to “Section 501(a)” in Section 41(b)(3)(C) of the
14 Internal Revenue Code, relating to contract research expenses, is
15 modified to read “this part or Part 10 (commencing with Section
16 17001).”

17 (h) (1) For each taxable year beginning on or after January 1,
18 2000:

19 (A) The reference to “3 percent” in Section 41(c)(4)(A)(i) of
20 the Internal Revenue Code is modified to read “one and forty-nine
21 hundredths of one percent.”

22 (B) The reference to “4 percent” in Section 41(c)(4)(A)(ii) of
23 the Internal Revenue Code is modified to read “one and
24 ninety-eight hundredths of one percent.”

25 (C) The reference to “5 percent” in Section 41(c)(4)(A)(iii) of
26 the Internal Revenue Code is modified to read “two and forty-eight
27 hundredths of one percent.”

28 (2) Section 41(c)(4)(B) shall not apply and in lieu thereof an
29 election under Section 41(c)(4)(A) of the Internal Revenue Code
30 may be made for any taxable year of the taxpayer beginning on or
31 after January 1, 1998. That election shall apply to the taxable year
32 for which made and all succeeding taxable years unless revoked
33 with the consent of the Franchise Tax Board.

34 (3) Section 41(c)(7) of the Internal Revenue Code, relating to
35 gross receipts, is modified to take into account only those gross
36 receipts from the sale of property held primarily for sale to
37 customers in the ordinary course of the taxpayer’s trade or business
38 that is delivered or shipped to a purchaser within this state,
39 regardless of f.o.b. point or any other condition of the sale.

1 (4) Section 41(c)(5) of the Internal Revenue Code, relating to
2 election of the alternative simplified credit, shall not apply.

3 (i) Section 41(h) of the Internal Revenue Code, relating to
4 termination, shall not apply.

5 (j) Section 41(g) of the Internal Revenue Code, relating to
6 special rule for passthrough of credit, is modified by each of the
7 following:

8 (1) The last sentence shall not apply.

9 (2) If the amount determined under Section 41(a) of the Internal
10 Revenue Code for any taxable year exceeds the limitation of
11 Section 41(g) of the Internal Revenue Code, that amount may be
12 carried over to other taxable years under the rules of subdivision
13 (f), except that the limitation of Section 41(g) of the Internal
14 Revenue Code shall be taken into account in each subsequent
15 taxable year.

16 (k) Section 41(a)(3) of the Internal Revenue Code shall not
17 apply.

18 (l) Section 41(b)(3)(D) of the Internal Revenue Code, relating
19 to amounts paid to eligible small businesses, universities, and
20 federal laboratories, shall not apply.

21 (m) Section 41(f)(6) of the Internal Revenue Code, relating to
22 energy research consortium, shall not apply.

23 (n) A taxpayer may sell a credit allowed under this section
24 pursuant to Article 4.5 (commencing with Section 12097) of
25 Chapter 1.6 of ~~Part~~, *Part* 2 of Division 3 of Title 2 of the
26 Government Code.

O